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ORIGINAL

EX PARTE OR LATE FILED

RECEIVED
JUN 18 2001
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

June 18, 2001

Ex Parte

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: In the Matter of Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers, CC Docket 96-98

Dear Ms. Salas:

Enclosed please an original and find four copies of the Emergency Petition for Stay of Order filed on behalf of Mpower Communications Corp. and North County Communications, Inc. for filing in the above-captioned proceeding.

Please contact me at (202) 955-9871 if you have any questions regarding this filing.

Sincerely,

David A. Konuch

Enclosures

cc: Dorothy Attwood
Alex Starr
A.J. DeLaurentis

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EX PARTE OR LATE FILED **ORIGINAL**

Before the
Federal Communications Commission
Washington, D.C. 20554

RECEIVED
JUN 18 2001
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Access Charge Reform	)	**CC Docket No. 96-262**
	)	
	)	
Reform of Access Charges Imposed by Competitive Local Exchange Carriers	)	

EMERGENCY PETITION FOR STAY OF ORDER

Jonathan E. Canis
David A. Konuch
KELLEY DRYE & WARREN LLP
1200 19th Street, N.W.
Suite 500
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(202) 955-9600

Dated: June 18, 2001

SUMMARY

Mpower Communications Corp. and North County Communications, Inc. (hereinafter "Petitioners") hereby respectfully request that the Federal Communications Commission ("Commission") stay its *Seventh Report and Order in CC Docket No. 96-262* (the *"Order"*). Specifically, Petitioners seek a stay of the Order's provisions (i) that immediately prescribe the rates that competitive local exchange carriers ("CLECs") may charge for their tariffed access services; (ii) that require CLECs entering a new service area to charge an access rate no higher than that of the incumbent local exchange carrier ("ILEC") operating in the same geographic area; and that force CLECs to lower their interstate access rate to the rate of the ILEC operating in the same geographic area after a four-year transition period.

The *Order* is profoundly flawed, both as a matter of law and public policy. First, the *Order* effectively prescribes the rates that CLECs may charge for their access services without any consideration of the CLEC's costs of providing service. The Commission's failure to consider the CLECs' actual costs is arbitrary and capricious, and effects an unconstitutional taking. Second, the rule requiring CLECs providing service in a new MSA to mirror the ILEC's interstate access rate has no basis whatsoever in the record of this proceeding. As such, it is arbitrary and capricious, effects an unconstitutional taking, and violates the Administrative Procedure Act. Moreover, even if the record of this proceeding did support adoption of such a rule -- and it does not -- implementation of that rule is impossible as a practical and technical matter because CLECs are incapable of billing different rates on an MSA-specific basis. Third, the Commission has discriminatorily prohibited CLECs from recouping all of their costs of call origination and termination through per minute access charges on the same basis as it permits ILECs to do so. This departure from the Commission's longstanding precedent holding that a

carrier is entitled to recover its reasonable costs of providing service is arbitrary and capricious and violates the Fifth Amendment.

Petitioners clearly satisfy the applicable legal standards used by the Commission in determining whether grant of a stay of the *Order* pending reconsideration or judicial review is appropriate, and will seek a stay from the court of appeals if their request is not granted.

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Access Charge Reform	)	**CC Docket No. 96-262**
	)	
	)	
Reform of Access Charges Imposed by	)	
Competitive Local Exchange Carriers	)	

EMERGENCY PETITION FOR STAY OF ORDER

Pursuant to Rules 1.41 and 1.44(e) of the Commission's Rules, 47 C.F.R. §§ 1.41, 1.44(e), Mpower Communications Corp. and North County Communications, Inc. ("Petitioners") hereby respectfully request that the Federal Communications Commission ("Commission") stay its Seventh Report and Order in the above referenced docket, released April 27, 2001.[1] Specifically, Petitioners seek a stay of the Order's provisions (i) that immediately prescribe the rates that competitive local exchange carriers ("CLECs") may charge for their tariffed access services; (ii) that require CLECs entering a new service area to charge an access rate no higher than that of the incumbent local exchange carrier ("ILEC") operating in the same geographic area; and (iii) that force established CLECs to lower their interstate access rate to the rate of the ILEC operating in the same geographic area after a four-year transition period. As set forth

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[1] *Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket 96-262, Seventh Report and Order and Further Notice of Proposed Rulemaking, FCC 01-146 (April 27, 2001) ("*Order*").

below, Petitioners clearly satisfy the applicable legal standards used by the Commission in determining whether grant of a stay of the *Order* pending reconsideration or judicial review is appropriate.

This Petition is submitted on an emergency basis, requesting the Commission's immediate attention. If the Commission does not act to stay its *Order* by June 20th, 2001, Petitioners will consider such inaction to constitute a rejection of their Petition. If this Petition is rejected by the Commission, the Petitioners intend to seek appropriate relief before the District of Columbia Circuit Court of Appeals.

In its *Order*, the Commission, for the first time in its history, established rules directly regulating the access charges of competitive local exchange carriers ("CLECs"). The Commission ruled that in areas where CLECs provided service prior to the effective date of the *Order*, CLECs must reduce tariffed access charges from current levels to 2.5¢ immediately; then to 1.8¢ the following year, to 1.2¢ the year after that, to 0.55¢ thereafter. In addition, the Commission imposed a requirement whereby any CLEC that enters a new Metropolitan Statistical Area ("MSA") must immediately tariff the ILEC rate, even if the CLEC tariff higher rates in areas where it is currently providing service. This means that the 2.5¢ maximum rate that the Commission will impose upon the effective date of the *Order* would apply only to geographic areas where CLECs currently provide service; for new markets that CLECs enter, the *Order* requires that CLECs tariff the prevailing ILEC rate. For the largest ILECs, which serve most access lines in the country, the tariffed per-minute charge for access services is approximately 0.7¢.

The *Order* is profoundly flawed, both as a matter of law and public policy. First, the *Order* prescribes the rates that CLECs may charge for their access services –without any consideration whatsoever of the CLECs' costs of providing service. This failure to consider the CLEC's actual costs is arbitrary and capricious, and effects an unconstitutional taking. Second, the rule requiring CLECs providing service in a new MSA to immediately mirror the ILEC's interstate access rate has no basis whatsoever in the record of this proceeding, and was adopted without any opportunity whatsoever for review and comment by the public. As such, it is arbitrary and capricious, effects an unconstitutional taking, and violates the Administrative Procedure Act's ("APA's") notice and comment requirements. Moreover, even if the record of this proceeding did support adoption of such a rule – and it does not – implementation of that rule is impossible as a practical and technical matter because CLECs are incapable of billing different rates on an MSA-specific basis.

Third, the Commission has discriminatorily prohibited CLECs from recouping all of their costs of call origination and termination through per minute access charges, although it permits ILECs to do so. This inexplicable departure from the Commission's longstanding precedent holding that a carrier is entitled to recover its reasonable costs of providing service is arbitrary and capricious and violates the Fifth Amendment.

BACKGROUND

Congress enacted the landmark Telecommunications Act of 1996 to encourage CLECs to enter the market for local telephone services and provide an alternative to the Baby Bell companies that dominated that market for decades. Indeed, the purpose of the Act was:

> to provide for a pro-competitive, deregulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information

> technologies and service to all Americans by opening all telecommunications markets to competition . . . .[2]

In the years since the Act was signed into law, competitive local service providers have just begun to make significant inroads into the formerly monopoly services markets. Yet, the Commission has, through its *Order*, inexplicably adopted policies that are severely harmful to these new competitors. Instead of following its prior policies designed to allow nascent competition to take root, the Commission ignores the APA's requirements and its own past precedent in order to bestow competitive advantages to the carriers who require them the least: large IXCs and ILECs.[3] The Commission's *Order* conflicts with the APA and the 1996 Act and therefore must be stayed.

ARGUMENT

In reviewing a motion for stay, the Commission has followed the precedent of the United States Court of Appeals for the District of Columbia Circuit. *See In re Virgin Islands Tel. Corp.*, 7 FCC Rcd 4235, ¶ 13 (1992). Thus, the Commission may grant a stay when (1) the movant is likely to prevail on the merits; (2) the movant will likely suffer irreparable harm absent a stay; (3) others will not be harmed if a stay is issued; and (4) the public interest will not be harmed if a stay is issued. *See Washington Metro. Area Transit Comm'n. v. Holiday Tours, Inc.*, 559 F.2d 841, 842-43 (D.C. Cir. 1977); *TCI TKR of Georgia, Inc.*, Memorandum Opinion and

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2 S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess. at 1 (1996). *See also* Pub. L. No. 104-104, 110 Stat. 56, 56 (1996) (The purpose of the 1996 Act is "to promote competition").

3 For instance, according to AT&T, many of the calls carried by CLECs consist of originating 8YY traffic. *See Order* at ¶ 100. Yet, AT&T's end-user rate for this traffic greatly exceeds the CLEC access charges that it alleges are unreasonable. For instance, AT&T charges 45 cents per minute – more than 10 times the average per minute access charge it pays to CLECs – plus a $2.99 service charge for its heavily advertised 1-800-CALL ATT service. Rebecca Blumenstein, "Reform Act Hasn't Delivered Promises to Customers," Wall Street Journal, May 3, 2001 at B1.

Order, 15 FCC Rcd 445 (2000). As demonstrated below, the Petitioners' case satisfies each prong of this standard.[4]

I. PETITIONERS ARE LIKELY TO SUCCEED ON THE MERITS

The stated goal of the *Order* was to "to eliminate regulatory arbitrage opportunities that previously have existed with respect to tariffed CLEC access services" by forcing CLEC access rates to mirror those of the incumbent LECs.[5] Under the regime adopted by the Commission, CLEC access rates that are at or below the benchmark will be presumed to be just and reasonable and CLECs may impose them by tariff. Rates above the benchmark will be mandatorily detariffed. The Commission purported to adopt a "pro-competitive, deregulatory national policy framework" that would simultaneously resolve a number of issues related to CLEC's tariffed interstate switched access charges and eliminate regulatory arbitrage opportunities. However, as set forth below, the adoption of the rules set forth in the *Order* violates the APA's notice and comment requirements and presents other implementation problems.

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4 The D.C. Circuit has emphasized that these factors relate on a "sliding scale," such that when "the arguments for one factor are particularly strong, an injunction may issue even if the arguments in other areas" are less compelling. *See Serono Labs v. Shalala*, 158 F.3d 1313, 1317 (D.C. Cir. 1998). This is particularly true where, as here, a stay request simply seeks to preserve the *status quo* pending judicial review. Indeed, the Commission itself has indicated that a stay maintaining the *status quo* should be granted "when a serious legal question is presented, if little harm will befall others if the stay is granted and denial of the stay would inflict serious harm." *Florida Publ. Serv. Comm'n*, 11 FCC Rcd 14324, 14325-26 & n.11 (1996); *see also Washington Metropolitan*, 559 F.2d at 844 ("An order maintaining the *status quo* is appropriate when a serious legal question is presented, when little if any harm will befall other interested persons or the public and when denial of the order would inflict irreparable injury on the movant. . . . [Such relief is available] whether or not movant has shown a mathematical probability of success.").

5 *Order*, ¶ 3.

A. The Commission's Adoption of a Rule Restricting the Availability of the Transitional Benchmark to MSAs Where CLECs Are "Actually Serving Customers on the Effective Date" of the Order Is Arbitrary and Capricious, a Clear Violation of the APA and Is Impossible to Implement

In its *Order* the Commission adopted a tariff benchmark rate for CLEC interstate switched access rates that may be charged by a particular CLEC by tariff to the lower of: (1) 2.5¢ per minute, or (2) the lowest rate that a CLEC has tariffed for access, during the 6 months immediately preceding the effective date of the *Order*.[6] The Commission determined that "any rate above this level (unless it is still below the competing ILEC's rate) will be conclusively deemed to be unreasonable in any proceeding challenging the rate."[7] However, the Commission concluded that the benchmark rate should be available only in areas where a CLEC was actually serving customers as of the effective date of the *Order*. The Commission's justification for adoption of this rule – which was presented for the first time in the *Order*, was never set out for comment, and is completely unsupported in the record – was its finding "that it is prudent to permit CLECs to tariff the benchmark rate for their access services only in the markets where they have operations that are actually serving end-user customers on the effective date of these rules" in light of the "historical ability of CLECs to tariff access rates well above the prevailing ILEC rate may have contributed to economically inefficient market entry by certain CLECs."[8] Based on this rationale, the Commission restricted "the availability of the transitional benchmark rate to those MSAs in which CLECs are actually serving end users on the effective date of these rules." In MSAs where CLECs begin serving customers *after* the effective date of the *Order*, the

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6 *Order*, ¶ 56.

7 *Order*, ¶ 57.

8 *Order*, ¶ 58.

Commission concluded that CLECs may tariff rates only equivalent to those of the competing ILEC.[9] In most areas of the country, the prevailing ILEC rate is approximately 0.7¢ per minute.

The Commission's adoption of this rule constitutes a clear violation of the APA in that the Commission failed to provide adequate notice and comment on the rule restricting applicability of the "conclusively reasonable" benchmark access rate to those MSAs where a CLEC actually provides service to end users prior to the effective date of the Commission's *Order*. The APA (specifically 5 U.S.C. § 553(b)(3)) requires that "general notice of proposed rule making shall be published in the Federal Register," and shall include "either the terms or substance of the proposed rule or a description of the subjects and issues involved."[10] It is clear that the Commission's adoption of the "new MSA" restriction failed to comply with the APA's notice and comment requirements.

The Court of Appeals for the District of Columbia Circuit has interpreted the APA's notice requirements to serve three basic purposes: (1) improving the quality of agency rulemaking by testing proposed rules through exposure to public comments; (2) providing an opportunity to be heard, "which is basic to fundamental fairness"; and (3) allowing affected parties to develop a record of objections for judicial review.[11] Accordingly, agency notice "must describe the range of alternatives being considered with reasonable specificity. Otherwise, interested parties will not know what to comment on, and notice will not lead to better-informed agency decision making."[12] The Commission plainly failed to provide the requisite public notice

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9 *Order*, ¶ 58.

10 5 U.S.C. § 553(b)(3).

11 *See United Church Board for World Ministries v. S.E.C.*, 617 F.Supp. 837 (D.C.D.C. 1985) ("*United Church*").

12 *Id.*, at 839.

and opportunity for comment with regard to these newly-adopted rules, and there is no basis whatsoever for the Commission to claim that any exception to the APA's notice and comment rules is applicable here.[13]

The NPRMs that lead to the adoption of the *Order* failed to include any mention of the subjects and issues involved with "new MSA restriction" in connection with the Commission's proposal to adopt a benchmark CLEC access rate. Nor did a single commenter proposed such a rule in the entire record of this docket. The issues raised by the Commission in its *Fifth Report and Order and FNPRM,*[14] included only: "whether any statutory or regulatory constraints prevent an IXC from declining a CLEC's access services;"[15] whether the problem of excessive CLEC access rates might be "solved if IXCs charged different rates to end users within the same geographic area based upon the level of access charges levied by the end user's local exchange company;"[16] whether mandatory detariffing of CLEC interstate access charges might address any market failure to constrain terminating access rates;"[17] "whether the incumbent LECs' terminating access charges should serve as a benchmark to evaluate the reasonableness of CLECs' terminating rates" and what rates to use as a benchmark, *e.g.* the incumbent LEC rate in

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13 *See Reeder v. F.C.C.*, 865 F.2d 1289 (D.C. Cir. 1989) ("The APA's procedural rule exception is to be construed very narrowly, and it does not apply where the agency 'encodes a substantive value judgment.'"). There is no question that the newly-adopted rules "encode a substantive value judgment" – in fact, they radically change the way CLECs do business. Therefore, the Commission cannot legally evade the notice and comment requirements of the APA.

14 *Access Charge Reform*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, ¶¶ 188-189 (rel. Aug. 27, 1999) ("*Fifth Report and Order and FNPRM*").

15 *Id.*, ¶¶ 243, 244.

16 *Id.*, ¶ 244 (emphasis provided).

17 *Id.*, ¶ 246.

the area served by the CLEC, or some other terminating access rate."[18] In addition to the above, the Commission's *Fifth Report and Order and FNPRM* sought public comment on issues related to termination of access services in its 1999 decision in *MGC Communications v. AT&T Corp.*[19] However, nowhere in the Commission's *Fifth Report and Order and FNPRM* did the Commission propose or refer in any way to the possibility of an "MSA exception" to any proposal regarding establishing presumptively reasonable benchmark rates. Recently, the Commission again sought public comment on "whether and how to reform the manner in which competitive local exchange carriers (CLECs) may tariff the charges for the switched local exchange."[20] Again, the Commission did not mention or seek public comment on an MSA exception rule, nor did any commenter suggest the need for such a rule. There is simply nothing in the record of any prior order that would suggest or lead the public to believe that such a substantive rule might be forthcoming: it was entirely a surprise, without any basis or precedent.

Indeed, while the Commission has been considering issues surrounding termination of the IXC/CLEC relationship, as well as the possibility of instituting a mandatory detariffing or benchmark rate regime for CLECs, the Commission never once alluded to the possibility of instituting such a new MSA restriction in connection with the adoption of a benchmark rate. As the courts have consistently held, "a general request for comments is not adequate notice of a proposed rule change. Interested parties are unable to participate

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18 *Id.*, 14 FCC Rcd 14221, ¶ 247.

19 *MGC Communications v. AT&T Corp.* 14 FCC Rcd 11647 (1999) ("*MGC I*"), *aff'd. full Commission,* 15 FCC Rcd 308 (1999) ("*MGC II*").

20 Public Notice "Common Carrier Bureau Seeks Additional Comment on Issues Relating to CLEC Access Charge Reform, Pleading Cycle Established," DA 00-2751, CC Docket 96-262 (Dec. 7, 2000).

meaningfully in the rulemaking process without some notice of the direction in which the agency proposed to go." [21] Failure of the Commission to make known agency views at the time of publication of notice "circumvents the APA notice requirements" because "proposed rule changes cannot be tested when the public is unaware of both the proposed revision and the theory under which the agency makes its proposal."[22]

The complete absence of any mention of the proposal on the record of this proceeding is clear evidence of this fact, and even one diligently monitoring the comments and *ex partes* associated with this docket could not have reasonably commented on this issue.[23] While the adoption of a CLEC benchmark was clearly raised in previous notices, the *Order* itself was the first and only instance in which the new MSA restriction was raised by the Commission. There, the Commission merely attempted to provide justification for adopting the rule, stating that it felt it "important to ensure that this transitional mechanism serves that purpose, rather than presenting CLECs with the opportunity to enter additional markets in a potentially inefficient manner through reliance on tariffed access rates above those of the competing ILEC."[24] As courts have observed, "when interested parties are unaware that a rulemaking process will result in specific regulations, the purposes of the APA notice requirements cannot be served."[25]

One can rest assured that if the Commission had, in fact, observed the requirements of the APA and given any indication that they intended to adopt the rule exempting

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21 *See Forester v. Consumer Product Safety Commission*, 559 F.2d 774, 787 (D.C. Cir. 1977) (emphasis supplied).

22 *See United Church*, 617 F. Supp. at 840.

23 *See id.* at 839-840.

24 *Order*, ¶ 58.

25 *See United Church*, 617 F. Supp. at 841.

new MSAs from the applicable benchmarked switched access rate, the record of the proceeding would have been rife with comments opposing such a rule. As a result of the Commission's failure to follow the notice requirements of the APA, there was no opportunity for carriers to make the Commission aware of the implications of such a proposal. Specifically, carriers would have, no doubt, commented on the fact that as a practical and technological matter, implementation of the Commission's rule would be impossible due to the limitations of carrier billing systems, which do not accommodate MSA by MSA price distinctions.

In addition to this patent violation of the APA, the "new MSA" rule constitutes a rate prescription because it sets mandatory rate levels for CLEC access charges in new markets. This is also a flaw that characterizes the Commission's broader approach in the Order, and is not limited to the "new MSA" provision. The following section explains in detail that the Commission's prescription of CLEC access charges is arbitrary and capricious, discriminatory, and violative of the Constitution and the Act. These same arguments apply to the Commission's decision to compel CLEC adoption of the ILEC rates immediately upon entering new MSAs. Rather than repeat those arguments in this section, they are incorporated herein by reference.

Finally, the "new MSA" rule is impossible to implement. CLEC billing systems are incapable of billing different rates on an MSA-specific basis. Had the Commission put this issue out for comment, it certainly would have received extensive information demonstrating this to be the case. [26] As the *Order* now stands, there is no consideration of the technical ability of CLECs to comply with this order, and no discussion of the cost or time that it would take to

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[26] In an *ex parte* statement submitted on May 25, 2001, no less than five carriers submitted affidavits stating that CLEC billing systems are incapable of billing rates that differ on an MSA by MSA basis, and therefore, the Commission's "new MSA" rule could not be

. . . *continued*

modify CLEC billing systems to allow for such billing practices, if indeed such modifications are possible.

For all of the reasons discussed above, the Commission's "new MSA" rules are likely to be reversed on appeal.

B. The Commission's Tiered Rate Structure Creates Barriers to Entry in Violation of the Act's Purposes

Section 253 of the Act provides the Commission with authority to preempt barriers to entry of the local telecommunications market erected by *states*. See 47 U.S.C. § 253. It follows from Section 253 that the Commission *itself* may not erect barriers that arbitrarily prevent certain carriers from entering the local exchange service market. Yet, the three-tiered pricing structure created in Commission's proposed rules erect just such a barrier.

The Commission's rules grant both large and small ILECs the ability to charge a compensatory rate. In contrast, the proposed rules limit CLECs to charging the ILEC rate, which may, but most likely, is not compensatory to those carriers. By allowing ILECs to charge a compensatory rate while requiring CLECs to charge rates that may or may not be compensatory to those carriers because of their entirely disparate economies of scale, cost structures, networks and financing.[27] By allowing ILECs to charge a compensatory rate while requiring CLECs to

implemented by June 20, 2001. *See Ex parte*, Letter from Jonathan E. Canis, Kelley, Drye & Warren, to Magalie Roman Salas, FCC, May 25, 2001.

27 Although it concededly cannot be stated for certain with respect to any particular CLEC that the newly-adopted rates are, or are not, compensatory (to do so would require a full-blown cost study), it can be stated with certainty that there is no demonstrable relationship between an ILEC's access rate and a CLEC's cost of providing access services. Perhaps even more importantly, the Commission did not even bother to explore what the CLECs' actual cost of providing access service is, instead merely prescribing the rate used by an unrelated entity with entirely different economics. This is on its face entirely arbitrary.

charge rates that may or may not be compensatory, the rules provide ILECs with a competitive advantage over CLECs.

The effect of the per minute rate cap is to allow ILECs a head start over new entrants for cost recovery. This advantage is, of course, over and above other unearned advantages that the ILEC started out with, such as years of amortizing its rate base over monopoly rate payers, and the ability to control the speed and cost at which the CLECs obtain inputs such as collocation and local loops needed to provide service. The Act was intended to level the playing field so that CLECs can compete against ILECs. Yet, the Commission's rule has the effect of perpetuating the ILECs' scale and scope advantages by providing them with new advantages, certainly a result that the Act's framers never intended.

Under the Commission's proposed rules, *all* CLECs are uniquely disadvantaged as compared to ILECs. The degree of the disadvantage depends arbitrarily on when the CLEC began providing service and where. In fact, the carriers facing the greatest disadvantage would be new entrants that have yet to serve any customers. It is almost as if the Commission is trying to *prevent* market entry, as opposed to encouraging it as the Act requires.

In essence, the Commission's rules create a three-tiered system of preferences based on when and where the carrier began providing service. Under the Commission's rules, the ILECs represent a preferred class of carriers permitted to charge rates that the Commission, overseen by the courts, has determined are compensatory. The Commission's rule then creates a second class of carriers, CLECs who already serve certain markets, which may charge the Commission's benchmark rate, followed by annual rate reductions in subsequent years. Finally, the rules create a third class, CLECs who have the misfortune of not yet beginning to serve customers, or those that are expanding into new MSAs. Those carriers must immediately begin charging the ILEC rate.

It is unclear whether the rates the Commission permits these CLECs to charge will be compensatory, as they are based solely on the ILEC's per minute rate, minus any scale economies that the ILECs reap by possessing the lion's share of all customers. The Commission's rules already allow the ILECs to earn a compensatory rate and spread their costs over their larger customer base, thereby providing them with advantages over CLECs. However, the rules provide the second class of CLECs with advantages over the third class based solely on the arbitrary factor of which market they began providing service in and when. Such an approach is completely inconsistent with the 1996 Act, which seeks to *remove* barriers to entry. so that all carriers can compete on a level playing field.[28]

The 1996 Act was designed to create robust competition, not to divide carriers into preferred classes by regulatory fiat. To level the playing field between competitors, the Act's provisions such as § 251 attempt to remove the inherent advantages possessed by ILECs. The Commission's rules do just the opposite, by creating *new* advantages for ILECs. The Commission's rules, by allowing different classes of carriers to charge different rates – to allow ILECs to charge rates determined to be compensatory while requiring CLECs to match the rates despite fewer scale economies – is anticompetitive and unreasonably discriminatory. The Act

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28 Yet another class of carriers would be rural CLECs, which the Commission permits to charge rates that are more in line with their costs. *Order* at ¶ 66. There, the Commission refers to the higher costs these carriers face as a result of low customer densities. However, the Commission never addresses the argument that all CLECs face similar densities, especially in their buildout phase, *see* ALTS Comments at Attachment 1 ("QSI Consulting Report on CLEC Cost Issues and Survey of CLEC Interstate Access Rates") ("QSI Report") at 3, 5, which explains why most CLECs charge rates closer to those of NECA carriers and independent ILECs.

is about opening markets and competitive neutrality. A regime that confers additional advantages to ILECs and throws additional hurdles into the path of new entrants does violence to the intent of Congress.

C. The Commission Has Engaged in Impermissible Rate Prescription

In the *Order*, the Commission ruled that in areas where CLECs provided service prior to the effective date of the *Order*, CLECs must reduce access charges from current levels to 2.5¢ immediately; then to 1.8¢ the following year, to 1.2¢ the year after that, to 0.55¢, the ILEC rate, thereafter. In so doing, the Commission departed from recent, prior precedent in which it declined to regulate directly CLEC access rates, *see Hyperion Telecommunications, Inc. Petition for Forbearance*, Memorandum Opinion and Order, 12 FCC Rcd 8596 (1997), s*ee also Access Charge Reform Fifth Report and Order*, 14 FCC Rcd 14221 (1999), and other recent precedent which ruled that a CLEC's rate is not per se unreasonable merely because it exceeds the ILEC rate.[29] In adopting an initial benchmark rate of 2.5¢, the Commission noted that both the IXCs and ALTS, the major trade association representing CLECs, agreed on this initial number. *Order* at ¶ 50. However, the Commission failed to discuss the fact that the ALTS plan was part of a package that resulted in rate reductions to a tariffed rate above the ILEC rate, allowed CLECs serving smaller markets to establish considerably higher rates, allowed all CLECs to establish higher rates if they could be justified by a cost showing, and required the issuance of FCC declaration ruling in support of CLECs' right to collect previously tariffed rates.[30]

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29 Order at ¶ 37.

30 *See* Order at ¶ 50. Petitioners Mpower (formerly known as "MGC Communications, Inc.") and North County are CLECs that charge more than 2.5 cents per minute of use ("MOU") for access services. The Commission has offered no basis for its choice of a 2.5 cent benchmark, other than the fact that it was suggested by ALTS as part of a broader compromise that did not involve requiring CLECs ultimately to charge the ILEC

. . . *continued*

The Commission never responded to the CLECs' showings that they faced higher costs than ILECs because they served a widely dispersed customer base and must purchase inputs *from* the ILECs in order to provide service.[31] Instead, the Commission implied that CLECs' costs were irrelevant, because the "competitive" rate would be any rate less than or equal to that charged by the ILEC. The Commission claimed that its prior policy of relying on the Section 208 Formal Complaint process to ensure the reasonableness of CLEC rates was not working, even though only two such complaints had been filed prior to issuance of the *Order*. Of those two, one complaint upheld a rate nearly three times the Commission's benchmark and the second – a rate complaint against BTI Communications -- had been filed so recently that the Commission's deadline for responding to the complaint had not yet passed.[32] Within a month after issuance of the *Order*, the Commission did resolve the rate case filed against BTI.[33] In the *BTI Rate Case Order* the Commission accepted BTI's view that CLECs, because of their relatively small number of customers served over a large area, resemble rural ILECs – the very

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rate. Neither North County nor Mpower were signatories to the so-called "GREAT" Plan sponsored by ALTS proposing this compromise. Both North County and Mpower submit that rates above the Commission's benchmark are supportable as just and reasonable. In fact, just last year the Commission refused to overturn Mpower's tariffed rates which at that time exceeded 7 cents per minute. *See Sprint Communications Co. L.P. v. MGC Communications, Inc.*, File No. EB-00-MD-002, FCC-00-206 (rel. June 9, 2000).

31 *See, e.g.*, ALTS Comments at 8-9; BayRing Safe Harbor Comments at 3; Focal & Winstar Safe Harbor Reply Comments at 8.

32 *See Sprint Communications Co. L.P. v. MGC Communications, Inc., cited supra* (upholding rate in excess of 7 cents per minute and refusing to adopt rule that rates above the ILEC rate are per se unreasonable); AT&T v. Business Telecom, Inc. c/w Sprint v. Business Telecom, Inc., filed January 17, 2001. The Commission also makes reference to three informal complaints. One of these, Sprint Communications Co. L.P. v. e.spire, settled several months prior to issuance of the *Order* at issue here.

33 *See AT&T v. Business Telecom, Inc.*, EB-01-MD-001, *consolidated with Sprint Corp. LP v. Business Telecom, Inc.*, EB-01-002, FCC 01-185 (rel. May 30, 2001) ("*BTI Rate Case Order*").

argument that the Commission *ignored* in its *CLEC Access Charge Order*.[34] The fact that the Commission based its decision in the BTI case this argument refused to even acknowledge it in the *CLEC Access Charge Order* demonstrates that the Commission acted arbitrarily and capriciously.

The Commission's attempt to justify its impermissible rate prescription fails on every level. The rules are flawed both on their merits and in the method in which they were adopted. The Commission disregarded the APA's dictates by ignoring its own precedent and evidence presented by commenters; violated the Constitution by mandating below cost rates; and improperly applied Supreme Court precedent governing industry-wide ratemaking. The Commission's action also runs afoul of the Act's prohibitions against discrimination by singling out CLECs for below cost rates while permitting all other local carriers to charge rates that recover their costs, and it violates the Act's policies designed to deregulate carriers and to increase local service competition.

1. The Commission's Rate Prescription Conflicts with *Permian Basin*

In attempting to justify its rate prescription, the Commission cites, but does not discuss *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968)("*Permian Basin*"), perhaps the most oft-cited case for the proposition that an agency may use a benchmark representing the costs or rates of a class of carriers when setting rates. However, in order to set rates based on benchmarks, the classifications of affected carriers must be narrowly drawn to include only those

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34 *BTI Rate Case Order* at ¶ 56. In fact, the arguments made were nearly identical. BTI, the defendant in the *BTI Rate Case* introduced the *same expert report* written by QSI Consulting that had been attached to the ALTS Comments submitted in this proceeding. *See* BTI's Amended Answer to the Second Amended Formal Complaint of AT&T at Attachment 4 ("QSI Consulting Report on CLEC Cost Issues and Survey of CLEC Interstate Access Rates"). *See supra note 27 (citing to QSI Report).*

similarly situated. Similarly situated carriers will not include those carriers with different levels of risks. Moreover, benchmarks are only lawfully set if based on a detailed record of the affected carriers' costs, and other attributes. In setting its benchmark, the Commission ignored evidence that CLECs were not similarly situated to ILECs, and failed to consider meaningfully the CLECs' costs.

In *Permian Basin*, the Supreme Court determined it was constitutional to set a maximum price for gas producers, based on the average costs of those producers to which the maximum rate was imposed, "without first evaluating the separate financial condition of each class." *Id.* at 769. In contrast to the Commission's action here, however, the agency in *Permian Basin* ultimately *did not* set maximum rates for all producers, but rather exempted the smaller producers from price controls. In reviewing whether the imposition of price controls was lawful, the Supreme Court noted that the exemption of the smaller producers properly recognized that they fell within a different classification from the large producers. Its determination was based on the conclusion of the examiner at the Federal Power Commission who had determined that the "basic difference between the small and large producer is that *the risks are materially different for each,*" *id.* at 786, n.50 (emphasis added), and thus they were dissimilar producers for purposes of setting rates.

A leading Commission case concerning access rate prescription, *Beehive Telephone Co., Inc.*, 13 FCC Rcd 12275 (1998) ("*Beehive*"), also recognizes that comparisons (and thus benchmarking) can only be done using the costs of *similarly situated carriers*. In prescribing a rate and revenue requirements for Beehive, in fact, the Commission emphasized that it was using a methodology based on industry averages *for comparably sized companies, with a comparable number of access lines*. *Id.* at 21.

Likewise, for purposes of performance benchmarking, the Commission has even found that all ILECs are not comparable. It notes, for example, that "the loop costs of an urban/suburban major ILEC may not be comparable to those of a small, rural LEC with longer average loops or less densely concentrated customers." [35] In fact, in finding that GTE and Bell Atlantic's performance could be benchmarked against one another, the Commission specifically recognized the importance of comparative geographic service area and customer dispersion.[36] However, the Commission never conducted this inquiry to determine whether CLECs and ILECs were similarly situated (and in fact ignored evidence that they were not similarly situated), and never meaningfully considered the CLECs' costs of providing service, in violation of prior ratemaking precedent.

The Commission's subsequent finding in the *BTI Rate Case Order* that CLECs most closely resemble small, urban ILECs underscores the arbitrary and capricious nature of the rate prescription in the *CLEC Access Charge Order*.[37] In the *BTI Rate Case Order* the Commission concluded that BTI most resembled a small, urban ILEC after examining the *same* QSI Consulting report that had been attached to ALTS' Comments in this proceeding. *See BTI Rate Case Order* at ¶ 57. The Commission stated, however, that this comparison was valid on a retrospective basis but not on a going forward basis. *See id.* at ¶ 59. The reason the Commission gave for not using the rates of small ILECs as a comparison to prescribe BTI's rates on a going forward basis was because "the *CLEC Access Charge Order* determined, based on a full record

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35 *See GTE Corporation,* 20 Communications Reg. 989 (rel. June 16, 2000), at ¶ 162.

36 *Id.* at ¶ 147.

37 In the *BTI Rate Case Order*, the Commission attempted to limit its finding to only BTI. However, the Commission pointed to specific evidence that BTI has a relatively small number of access lines spread over a large service area. As noted in the QSI Report, *see infra*, this customer dispersion pattern is typical of *most* CLECs.

and numerous competing considerations, what presumptively reasonable CLEC access rates will be in the future." *Id.* Yet, as demonstrated above, the Commission in the *CLEC Access Charge Order* neglected to consider or respond at all to the QSI Consulting Report containing arguments that it found dispositive in the *BTI Rate Case Order*. The two orders stand in conflict, despite the Commission's attempt at circular reasoning to incorporate the findings of the *CLEC Access Charge Order*, which did not address the CLECs' arguments concerning customer dispersion, into the *BTI Rate Case Order*, which not only addressed the arguments but found them persuasive. The law does not permit the Commission to engage in such "hide the ball" regulatory shell games. The Commission's finding that CLECs resemble small ILECs should have compelled it to use the rates of small ILECs as a benchmark *on a going forward basis as well*. Given the Commission's finding that the two types of carriers were similar, anything less would violate *Permian Basin*. Having found CLECs to resemble small ILECs, the Commission cannot then base their rates on those of *large* ILECs.

a. The Commission Failed to Consider Whether CLECs Were Similarly Situated to ILECs

In decreeing that all CLECs must set their rates at the ILEC rate, the Commission disregards its prior precedent, as well as the parties' arguments and the record before it in this proceeding. That record demonstrates unequivocally that CLECs are not similarly situated to the ILECs.[38] As set forth in the comments of ALTS and many individual commenters, CLECs employ optimally efficient technology, *see* QSI Report at 2, but nonetheless face higher costs than ILECs because of lower initial switch utilization and a less dense customer base, among other factors. *See* ALTS Comments at 9. As demonstrated by ALTS and other parties to this

[38] *See* ALTS Comments at 8-9.

proceeding, CLECs can be far more closely compared to rural LECs, with similar geographic scope and similar customer dispersion patterns.[39] Moreover, to provide service, CLECs must purchase inputs, such as Unbundled Network Elements and collocation, from the ILEC at a price that allows the ILEC to earn a profit. *See, e.g.*, ALTS Comments at 9. It goes against logic to suggest that CLECs, after purchasing these inputs from the ILEC, will be able to underprice the ILEC on access. This was the CLECs' primary argument in justifying higher rates than those of ILECs. Yet, the Commission's *Order* contains no rebuttal or any discussion whatsoever of this argument. The Commission does not state that CLECs are capable of meeting the ILEC rate based on an examination of CLECs' costs. Rather, it merely decrees that CLECs must meet the ILEC price regardless of whether this results in a below cost rate. Such conclusory statements do not satisfy the Commission's obligation of reasoned decisionmaking.[40]

The main difference between CLECs and ILECs is that ILECs serve virtually all of the customers in any given area. The argument that the CLECs made to the Commission is that density equals lower cost *only if you have all or most of the customers*. Instead of addressing the CLECs' argument that they possess customer densities that are lower than those of ILECs, the Commission merely assumes the opposite: that because a CLEC is operating in an

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39 The Commission recently credited this argument in the context of a complaint proceeding. *See AT&T v. Business Telecom, Inc.*, EB-01-MD-001, FCC 01-185 (rel. May 30, 2001) (comparing a CLEC to NECA carriers). As noted above, CLEC commenters made the same argument here, but the Commission failed to acknowledge it. The Commission's failure to acknowledge in the *CLEC Access Charge Order* an argument that it found dispositive in the *BTI Order* highlights the arbitrary and capricious nature of the rate prescription contained in the *CLEC Access Charge Order.*

40 *AT&T Corp. v. FCC*, 236 F.3d 729, 736-37 (2001) ("The FCC cannot silently depart from previous policies or ignore precedent") (*citing Committee for Community Access v. FCC*, 737 F.2d 74, 77 (D.C. Cir. 1984)); *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970)("an agency changing its course must supply a reasoned

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urban area, it must possess economies of scale similar to those of an ILEC. The Commission's implicit conclusion that any carrier operating in the same area as an ILEC will enjoy scale and scope economies similar to those of the ILEC (the parties are left to guess that this is the rationale for the Commission's rule as it is nowhere explained in the order) conflicts with both the evidence submitted in this proceeding, *see* ALTS Comments 8-9, and also with the Commission's prior – and recent -- holdings. *See Implementation of the Local Competition Provisions of the Telecommunication Act of 1996*, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd, 3639, ¶ 86, (1999) ("*UNE Remand Order*"). In fact, CLECs' relative lack of scale and scope economies, and customer densities that are similar to those of NECA carriers and rural independents explain why CLECs often charge in the same range as the NECA carriers (approximately 3.5 cents per MOU)[41] and rural independents, some of which charge in excess of 10 cents per minute -- rates which have been found to be reasonable by regulators. The Commission's discriminatory policy of preventing CLECs from recovering their costs while allowing ILECs to do so will not result in further efficiency, but will merely serve to perpetuate monopoly.

The Commission's holding also conflicts with rulings contained elsewhere in the *Order* that rural LECs – and rural CLECs face higher costs because they possess lower customer densities. *See Order* at ¶ 64. The Commission's failure to address this argument violates the APA, and the *Order's* internal inconsistency in its treatment of rural and non-rural CLEC costs represents arbitrary and capricious agency action.

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analysis indicating that prior policies and standards are being deliberately changed, not casually ignored").

41 *See* ALTS Comments at 7.

b. In Prescribing Rates, The Commission Misinterpreted Its Own Prior Holdings And By Its Own Admission Relied On Incomplete Evidence

In reaching the conclusion that an agency may have the authority to set rates based on benchmarks, the Supreme Court emphasized that benchmarking as a means of ratemaking was only "sufficient if the agency has before it representative evidence, ample in quantity to measure with appropriate precision the financial and other requirements of the pertinent parties." *Permian Basin*, 390 U.S. at 769. In *Permian Basin*, the Federal Power Commission had undergone almost eight years of proceedings. *Id.* at 824. During that time, it sent out three sets of questionnaires seeking detailed data on drilling and other costs, revenues and production, from the gas producers. When it finally set rates, it relied on data from responses to those questionnaires, as well as on a comprehensive study of historical costs of service submitted by its staff.

Similarly, in *Beehive Telephone Company, Inc.*, 13 FCC Rcd 12275 (1998), the Commission only set rates based on a benchmark, after a protracted series of tariff investigations looking into whether Beehive's access rates were set at reasonable levels. There, the Commission prescribed rates for Beehive Telephone Company only after several years of sequential attempts by Beehive to demonstrate that its rates were lawful, and based on an exhaustive examination of Beehive's own cost support data, and the costs of NECA carriers, of which Beehive was one.[42]

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[42] In disallowing certain of Beehive's expenses, the Commission relied on an extensive showing of potential wrongdoing, including the inclusion of such "expenses" as legal expenses that arose "from a divorce action filed against Beehive's president, litigation expenses associated with educational trust, and expenses for heating an airport hanger for Beehive's aircraft" in its development of rates. The Commission similarly disallowed Beehive's investment calculation; based on extensive evidence in the record that Beehive had not developed its costs "based on books and accounts maintained in accordance with

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In the instant case, the Commission misinterpreted the scant "anecdotal," evidence that existed concerning carrier rates, *see Order* at ¶ 47, and pointed out that other evidence submitted by parties was flawed. For instance, the Commission noted that information it primarily relied upon – that was submitted by AT&T, WorldCom, and Sprint – was flawed. *Order* at ¶ 47 n. 108, ¶ 49 n. 112. Yet, instead of seeking additional information that would correct these flaws, the Commission prescribed rates based on an admittedly incomplete and flawed record.

Moreover, the Commission's *Order* is inconsistent with findings on CLEC costs that the Commission made only recently. For example, in the Commission's *UNE Remand Order*, it found that CLECs incur costs that, by definition, were not incurred by ILECs. Specifically, the Commission found that CLECs must purchase UNEs from ILECs at rates higher than the ILECs' costs, and that CLECs had to purchase collocation from ILECs – and of course, ILECs did not have to purchase collocation from themselves.[43] In so finding, the Commission explicitly found the CLEC costs are higher than ILEC costs. Now, however, the Commission has required CLECs to charge no more than the ILEC rate – immediately in new MSAs, or over several years for other areas. To force CLECs to mirror the ILEC rate when CLECs incur costs higher than the ILEC's costs obviously forces CLECs to set rates at noncompensatory levels. The Commission, however, never even acknowledges its former findings, and certainly does not justify its reversal on these matters.

Part 32 of the Commission's Rules." 13 FCC Rcd at ¶ 21. Nor, according to the Commission, had Beehive explained why its net investment is approximately 55% higher than the "net investment of companies with a comparable number of access lines as Beehive" (emphasis added). *Id.* Instead of considering the CLECs' costs to provide service to determine whether CLECs and ILECs are similarly situated, the Commission has apparently taken the view that CLECs' costs are irrelevant.

Moreover, the Commission's *Order* is not flawed solely by an unexplained departure from its recent rulings – the *Order* is contradicted by another order that the Commission released on the same day. On April 27 – the day the FCC released the *Order* prescribing rates for CLEC access charges, it also released an order initiating a Notice of Proposed Rulemaking that proposed new rules governing all forms of intercarrier compensation.[44] In the *Intercarrier Compensation NPRM*, the Commission discusses at length the difficulty inherent in prescribing rates. Specifically, the Commission noted that, when networks contain high levels of common costs – such as the costs of local loops – it is difficult to know how those costs should be allocated among different services. The Commission said:

> There is no perfect solution to these cost allocation problems, largely because regulators cannot see individuals' demand functions. Any allocation that a regulator can make is arbitrary (in the economic sense), yet even a small allocation error can produce massive distortions.[45]

Yet this kind of distortive allocation of common costs is precisely what the Commission has done in its *Order*. The Commission has stated that, if CLEC costs are indeed higher than ILEC costs, "CLECs remain free to recover from their end users any greater costs that they incur in providing either originating or terminating access charges."[46] The Commission has therefore dictated that CLECs must allocate a higher percentage of their common costs away from services purchased by IXCs, and to services purchased by end users. On the same day that

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43 *See UNE Remand Order* at ¶¶ 261, 264-65.

44 *Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, FCC 01-132, CC Docket No. 01-92 (April 27, 2001) ("*Intercarrier Compensation NPRM*").

45 *Intercarrier Compensation NPRM*, FCC 01-132, ¶ 39.

46 *Order* at ¶ 39.

it made this ruling, however, it stated in the *Intercarrier Compensation NPRM* that such allocations are inherently arbitrary and potentially distortive. Thus, by its own admission, the Commission's prescription of ILEC rates for CLECs is arbitrary.

In sum, the Commission's *Order* noted that "precedent exists for setting rates by some means other than reviewing the costs of each individual industry participant."[47]. Regrettably for the competitive carrier industry and for consumers, the Commission has failed to follow this precedent. A stay must be granted to prevent the Commission's Rules from causing irreparable harm to competitive carriers and to competition.

2. The Commission's Order Violates the Fifth Amendment

In its *Order*, the Commission notes that because currently effective CLEC access rates were set by the CLECs themselves, "there should be no concern that the current rates provide an inadequate return to the carrier that tariffed them."[48] However, the Commission never discusses whether the rates that it is prescribing, which are less than the average rate charged by CLECs, would result in rates that are below cost.[49] Record evidence that the Commission ignored in this proceeding demonstrates that the rates are below cost, at least for some CLECs.[50] Requiring carriers to provide service at noncompensatory rates is a violation of

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47 *Order* at ¶ 46 (citing *Permian Basin*)

48 *Order* at ¶ 46.

49 The Commission's statement in footnote 105 of its *Order* that it is not setting rates, but rather is only "limit[ing] the rates that CLECs may impose through the tariff system" is disingenuous. The reason for this proceeding from the CLECs' point of view is because IXCs were refusing to pay CLEC access rates even when these rates *were* lawfully tariffed. *See Order* at ¶ 46 n.105.

50 *See Ex parte*, Letter to Magalie Salas, Secretary, FCC from Ross A. Buntrock on behalf of ALTS, CC Docket Nos. 98-63 and 96-262, March 28, 2001 at Attachment A: "Comparison of CALLS Local Switching Charges with UNE Rates." This document indicates that the UNE Platform rate exceeds the CALLS access rate in 25 states: Maine,

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the Fifth Amendment to the Constitution. *See Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989).

The obvious danger to competition posed by the Commission's approach is most clearly shown in an ex parte letter submitted by CLECs showing that the CALLS rate is *already below* the UNE platform rate in twenty-five states. This means that ILECs in these states are providing access service below their TELRIC rates, *i.e.*, below cost. In such states, CLECs would not be able to enter the market using the UNE platform, which is supposed to reflect the economies of scale gained by incumbents, in order to compensate CLECs for the inherent competitive advantages of scale and scope possessed by ILECs.

Creation of a regulatory regime, such as the Commission has done, that compels CLECs to lose money on each minute of access service carried simply cannot be squared with the Communications Act. It is black letter law that a carrier cannot be forced to offer a rate that threatens its ability to attract capital, and therefore, jeopardizes its very survival. *See id.* If this *Order* is not stayed, ILECs will be given unearned competitive advantages, to the detriment of CLECs and to telecommunications competition generally.

3. The Commission's Rules Are Anticompetitive and Result in Unreasonable Discrimination

Another serious flaw concerning the merits of the Commission's approach is the Commission's assertion that the ILEC rate is a "competitive" rate representing the rate of the most efficient carrier. However, as the Commission well knows, the ILEC rate was set by regulation, not competition. Most significantly, the CALLS ILEC rate was set as a result of an

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Vermont, New Hampshire, Massachusetts, Rhode Island, New Jersey, Delaware, Maryland, Virginia, West Virginia, Florida, Kentucky, Mississippi, Arkansas, California, Oklahoma, Arizona, Colorado, Indiana, Montana, Nebraska, North Dakota, South Dakota, Utah, Wyoming.

"unholy alliance"[51] between two of the three largest IXCs and all but one of the RBOCs. The CALLS rate resulted in lower access charges for IXCs, but was effectively revenue neutral for the RBOCs, because they were permitted to offset any decreases in per minute costs through increases in the SLC and through contributions from the Universal Service Fund. These rates were set through collusion between the established carriers, not by competition. Even so, ILECs were permitted to opt out of the CALLS rates if, after conducting a cost study, they felt that the CALLS rates provided them with insufficient revenue. However, as a result of the Commission's *Order*, CLECs have not been extended the same courtesy as the ILECs. While non-CALLS ILECs can continue to charge above the CALLS rate in its region, CLECs operating in CALLS ILEC territories will be compelled to charge the CALLS rate. As a result, the Commission's rule is both unreasonably discriminatory and anticompetitive.

Moreover, as the Commission recently recognized (but has ignored in its current order), it is clear that the ILEC is not the most efficient provider, and therefore, the alleged benefits to economic efficiency to be gained by pegging CLEC rates to the ILEC rate are illusory. As the Commission recently held in the *UNE Remand Order*, the incumbent LECs' "cost advantages and superiority of economies of scale, scope, and ubiquity [are] . . . a result of their historic, government-sanctioned monopolies." *UNE Remand Order* at ¶ 86. According to the Commission:

> These economies are now critical competitive attributes and would belong unquestionably to the incumbent LECs if they had "earned" them by superior competitive skills.

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51 *See* Telecommunications Reports, "Affordability of SLC, Consistency of FCC Policy Dominate Argument over Access Charge Rules," May 14, 2001 at 5 (quoting Judge Ellison of the Fifth Circuit Court of Appeals describing CALLS as an "unlikely—maybe even unholy—alliance.") The statement was made during oral argument of a case filed by consumer advocates challenging the SLC increase effected by CALLS.

> These advantages of economies, however, were obtained by the incumbents by virtue of their status as government protected monopolies.

UNE Remand Order at ¶ 86.

The Commission ignored its prior holding that the historical benefits gained from monopoly status should not belong to the ILEC. Allowing ILECs, but not CLECs, to reap these benefits is anticompetitive and results in unreasonable discrimination.

II. APPELLANTS WILL SUFFER IRREPARABLE HARM ABSENT A STAY

Absent a stay, Petitioners will suffer a variety of harms cannot be remedied, even if the FCC's rules are ultimately overturned at some point in the future. It is not simply a matter of recouping funds at a later date, because the multifarious nature and extent of the harm that will be done by the imposition of these new rules makes it very unlikely that even a resolution favorable to Petitioners could adequately address the damage to Petitioners' businesses in the interim.

The potential for damage to Petitioners' businesses is severe and multifaceted. First, as noted above, imposition of the rules will immediately result in placing all CLECs that enter new markets in violation of the law on a continuing basis for an indefinite period, because at present CLECs such as Petitioners are incapable of complying with the rules. It is unknown how long it will take to establish a billing system that can distinguish between MSAs for access rate purposes. Thus, Petitioners, and doubtless all other CLECs, to the extent they plan to enter new markets risk violating the rules almost indefinitely, possibly subjecting themselves to forfeitures and other sanctions, because they can do no other. Apart from any other consideration, this practical consideration -- that it is impossible to comply with the rules at present, necessarily compelling CLECs to be lawbreakers to the extent they enter new markets -- should warrant staying their effect.

Second, even if there were a present means of complying with the rules, there are many damaging aspects of the rules that do not have a suitable remedy at law. For example, by discriminating between existing and new markets, the rules have the effect of penalizing CLEC entry into new markets. Since it is extremely unlikely that a new market entrant can have the same cost structure and economies of scale as the dominant ILEC that has monopolized that market for a century, new markets can only be entered at a CLECs' peril, because it requires a commitment to provide competitors access to the new entrants' network at non-compensatory prices. From the Petitioners' point of view, this essentially requires a re-write of their business plans, and a reconsideration of expansion into new markets. This wholesale revamping of a business plan is not the sort of thing that can be compensated for later, since the inability to follow a planned expansion into other markets is likely to have a synergistic effect on the entire operations of a company. And, of course, it is unknown what financial effect it would have had to enter a market if the barriers placed by the new rules were not in effect. For one thing, since "timing is everything" in the dynamic competitive telecommunications world, it is entirely possible that if Petitioners delay or avoid entry into a given market due to these new restrictions, it is entirely possible that the competitive landscape for that market will have changed dramatically – and in an adverse fashion – the next time the opportunity comes around again. So even if the rules are ultimately struck down, there is no guarantee that Petitioners can recoup what they have lost in the interim, absent a stay.

Third, the new rules also create a very unfair competitive scenario in which CLECs are forced to lower their access rates to the rates of the prevailing ILEC in a given market they are entering for the first time, although their cost structures are very likely to make these access rates non-compensatory. This puts unfair pricing pressure on CLECs that must either refrain from entering a new market, or be compelled to lose money on an open-ended basis on access services, while at the same time directly competing for customers with the ILEC. Although concededly the ILEC charges the same access rates as the new entrant, this is nevertheless an unbalanced situation, because these rates are compensatory to the ILEC with its inherent economies of scale, but are destructive to the business of the higher-cost CLEC that must provide access services at a loss. As above, absent a stay there is no guarantee that Petitioners or any other CLEC subject to these pressures could recover even in the event of a complete victory in court.

The markets in which CLECs compete are not static; they are a moving target. If customers and opportunities are lost because of cost pressures that make CLECs unable to compete with ILECs and NECA carriers for price, these customers and opportunities may not come around again. This is particularly true of the large and medium business customers that CLECs especially target, but that are prone to entering into long-term, volume discount contracts for services. It would be harmful enough if this loss of potential business were the only harm, but the unfair competitive conditions imposed by the Commission's new rules have a "chain reaction" effect. If Petitioners cannot expand their businesses, they cannot grow their revenues. This makes them less attractive to sources of finance, potentially resulting in higher financing costs. This in turn further undercuts their financial position, leading to a spiraling series of problems. Without good sources of available financing at reasonable rates, a CLEC cannot afford to operate efficiently, or make investments in new equipment and technology necessary to attract the best customers, or provide the best customer service. Then in turn the expansion of the customer base suffers, there is possible reputation damage, etc. These are not harms that can be fully addressed simply by the payment of money. They can have a profound and permanent effect on a carrier's business prospects.

Courts have recognized that unrecoupable losses resulting from such unfair competition are the epitome of irreparable harm. *See Independent Bankers Ass'n of Am. v. Smith*, 534 F.2d 921, 929 (D.C. Cir. 1976). *Washington Metropolitan Area Transit Commission v. Holiday Tours, Inc.*, 559 F.2d 941, 843, n.2 (D.C. Cir. 1977) (noting that the destruction of a business is an essential economic injury and not a "mere" economic injury that is insufficient to warrant a stay). Absent a stay, Petitioners and other CLECs will be profoundly damaged in ways that are simply impossible to quantify and cannot be remedied at law.

III. NO OTHER PARTY WILL BE HARMED IF STAY IS GRANTED

If the Commission's *Order* takes effect, thereby forcing Petitioners to charge below cost rates and preventing them from expanding into new markets, Petitioners will suffer irreparable harm. Additionally, consumers will be harmed as the Commission's *Order* will compel price competitive providers of local exchange service to exit the market. In contrast, allowing Petitioners to continue to charge in excess of the ILEC rate for per minute access charges will not result in higher long distance rates because the total dollar of amount of CLEC access charges assessed to IXCs represents but a minuscule amount of those carriers' total spending on access charges.[52] Nor will a rate above the ILEC rate be unreasonable. IXCs will continue to pay billions of dollars in access charges that exceed the CALLS ILEC rate to non-CALLS ILECs after the Commission's *Order* takes effect. However, the Commission has never held that the higher rates of the non-CALLS ILECs are unreasonable and, apparently, has no future plans to do so. Accordingly, a stay will not harm others, and will serve the public interest.

Grant of a stay will maintain status the quo, and will preserve the regulatory environment that has been in effect since the inception of the competitive local services industry

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52 The Commission's order cites AT&T's claim that allegedly unreasonable CLEC access charges compel it to pay 100 million in charges above the ILEC rate each year. Order at ¶ 22. In contrast, the total amount of access charges paid to all LECs is nearly $28 billion. Industry Analysis Division, Federal Communications Commission Carriers, Statistics of Communications Common at 130 (Table 2.13) (2000). In addition, AT&T's claim that CLEC access rates are unreasonable is not credible. AT&T's own CLEC affiliate, a company called ACC National Telecom Corp., charges nearly 9 cents per minute, or more than twice the average rate that AT&T claims it pays to CLECs. ALTS Comments at 7.

15 years ago. No IXC can credibly argue it is subject to irreparable harm by continuation of status quo.[53]

When the FCC deregulated carriers it formerly found dominant – AT&T for long distance service, and the BOCs for high capacity circuits, it expressly found that the 208 complaint process provided other parties protection against unreasonable rates. That same rationale provides protection to any party now, and the FCC's departure from its earlier rationale in the context of CLECs is wholly unexplained. Finally, the two IXCs that have complained most loudly about CLEC access charges – AT&T and Sprint – are currently engaging in unlawful self help by refusing to pay lawfully tariffed charges. These carriers, having failed to pay any of the allegedly unreasonable rates, cannot be heard to complain of harm.

IV. STAY OF THE COMMISSION'S PATENTLY FLAWED AND ARBITRARY ORDER WILL SERVE THE PUBLIC INTEREST

Implementation of the Commission's *Order* threatens immediate harm to competitive local service providers. The Commission's *Order* will, upon effect 30 days after publication in the Federal Register, reduce access charges of the AVERAGE CLEC by nearly

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53 The Commission's assertion that Section 254(g) of the Act (mandating geographic rate averaging for IXCs) prevents IXCs from recovering from customers the costs of higher access rates has Congress's intent exactly backward. It is no answer for the Commission to prohibit charging compensatory rates because Section 254(g) prevents IXCs from recovering the true cost of providing the service. Rather, Congress enacted 254(g) because it intended that *IXCs* absorb the cost of higher rates that result from a customer's geographic location and to charge the same rate to all customers regardless of where the consumer lives. It is not the Commission's place to second guess Congress's conclusion concerning this cost allocation. Moreover, it is clear that consumers directly benefit when a CLEC offers them lower rates for local service. In contrast, IXCs have no obligation to pass on access rate savings in the form of lower rates, and the evidence demonstrates that they are not doing so. *See Reform Act*, *cited supra*, at B1 ("AT&T charges 45 cents a minute and a $2.99 service charge for those dialing its 1-800-CALL ATT service. Those who simply dial 0 and the phone number are slapped with a $4.99 service charge per call, plus a rate of 89 cents a minute.")

50%, and some CLECs by almost 80%.[54] As recent press accounts indicate, these carriers already are in fragile financial health. *See, e.g.*, *Wrong Numbers*, *cited supra* n. 46. Three of the carriers initially involved in lawsuits seeking to enforce their lawfully tariffed access rates against self-help measures have filed for Chapter 11 bankruptcy, and requiring such drastic rate cuts will accelerate this problem. As discussed above, in this time of unprecedented capital shortage, such draconian revenue reductions will drive some CLECs out of business. The Commission's rules will force those carriers not driven out of business to provide service below cost, effecting an unconstitutional taking that will cripple their ability to invest in new technology and expand into new services and markets.

If allowed to take effect, the Commission's rules will also provide dominant incumbents an insuperable advantage over their competitors, thereby creating an immediate barrier to competitive entry. As mentioned above, the new MSA rule will effect reductions of 80% in rates of the average CLEC in new markets, effectively forcing below-cost pricing and preventing entry into new markets. The public interest in opening markets and encouraging entry by competitors is a principal purpose of the Act. Rules that have the effect of crippling CLECs, the only carriers capable of providing local service competition, will harm the public interest. Yet, the Commission never attempts to balance the harm done to competition with the good it seeks to promote – alleged economic efficiency in access pricing.

In fact, as demonstrated above, no economic efficiency will result from requiring CLECs to charge the same rate as the ILEC, as the ILEC possesses additional scope economies

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[54] The average rate of CLECs participating in QSI's survey of CLEC access rates was 4.27 cents per minute of use (MOU) originating and 4.26 cents per MOU for terminating access service. The highest rate of which Petitioners are aware is the nearly 9 cent per minute rate charged by AT&T's CLEC affiliate, ACC.

that the CLEC cannot match. Even use of the UNE platform, designed to provide CLECs with the same scale and scope economies as ILECs, will not allow CLECs to match the ILEC rate in 25 of the 50 states, and provides CLECs with so slim a profit margin in others as to make the effort futile. The obvious economic consequence of such a pricing regime will be market exit by current competitors, and a guarantee that no new competitors take their place. The harm to the public interest will be very real when customers now receiving local service at a discount off the ILEC rate are forced to return to the ILEC as CLECs exit the market, in contravention of the Act's promise. If allowed to take effect, the Commission's *Order* will result in immediate harm to the public interest and, accordingly, it must be stayed.

V. CONCLUSION

Petitioners have demonstrated that, due to the Commission's unexplained deviation from its prior precedent and other violations of the APA, Petitioners are likely to succeed on the merits, and that, if the rules are allowed to take effect, Petitioners will suffer irreparable harm. In contrast, if a stay is granted, other parties will not be harmed, and the public interest will benefit. Therefore, Petitioners' request for stay must be granted.

Respectfully submitted,

By:__________________________

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Dated: June 18, 2001

CERTIFICATE OF SERVICE

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